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A Canadian Priorities Agenda: Ensuring Future Prosperity

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The IRPP's *Canadian Priorities Agenda* project was the inspiration for the 2008-2009 capstone seminar in the MPP program of the School of Public Policy and Governance at the University of Toronto. Taught by Wendy Dobson and Carolyn Hughes Tuohy, two of the judges in the original IRPP project, the course was offered in an intensive format as a core requirement in the final semester of the two-year program. The *Canadian Priorities Agenda* volume formed the basic text for the course, supplemented by readings chosen by the two instructors and guest presenters. The students took the role of judges; and the final assignment was the preparation of a 5,000-word paper, modeled on the judges' reports in the original project, making the case for an agenda comprising five policies selected from options presented in the course.

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A FRAMEWORK FOR CANADA'S FUTURE

The Canadian Priorities Agenda project as developed by the University of Toronto master's in public policy capstone course outlines 12 broad policy areas requiring action. Several themes emerge from the project that demand a comprehensive package of policy options as Canada moves forward. Domestically the experience of a globalizing economy in a liberal welfare state has resulted in unequal burden of costs and rising income inequality. Simultaneously, open markets and the advantages of trade have restructured our economy, while producing wealth for those at the top. The emergence of India and China has shaken the foundations of the economic order, demanding a new strategy for Canada. The unequivocal evidence that climate change is upon us has also placed new constraints on the country, and we can no longer justify ignoring our role in world greenhouse gas (GHG) emissions. Recognizing the challenges and opportunities facing Canada in the domestic and global context, my policy package will prioritize five options to be implemented to ensure the future prosperity of all Canadians.

THE EFFICIENCY-EQUITY TRADE-OFF

The pursuit of policies that promote economic efficiency can come at the expense of ensuring equitable distribution of wealth and/or goods and services. A policy package that does not address this trade-off in a balanced way risks being either unduly unfair, with long-run implications for social cohesion, or dismissed as "pie in the sky," with no long run strategy to maintain social programs. Addressing this trade-off, while simultaneously recognizing the need to strategically reposition Canada globally, is the central challenge for the design of a policy agenda that will sustain and enhance the future prosperity of all Canadians.

A sound approach must recognize the systemic barriers that prevent people from accessing the opportunities of a dynamic economy, while recognizing that social exclusion has implications for

future economic growth. There are several policy areas that are key to achieving a long-term strategy that is both economically efficient and equitable.

Policies that are rooted in "endogenous growth" theory address innovation, human capital accumulation and technological advancement, and are necessary to provide greater long-term social returns (Dolowitz 2004, 217). This theory assumes "that there are factors underlying economic growth internal to the market, and that economic growth (or decline) depends on factors, which transform the very economic system that created them" (Dolowitz 2004, 217). Departing from neoliberal models, a policy approach that adheres to endogenous growth theory assigns an active role for government "to correct the tendency of the unregulated market to under-invest and neglect the economic importance of social investment" (Dolowitz 2004, 218). In line with Dan Trefler's paper on productivity (2008), policies that facilitate human capital development have important implications for dealing with the nexus between efficiency and equity.

One limitation of a policy package that adheres mainly to the precepts of an endogenous growth theory is the long-term nature of the strategy. A policy package that focuses primarily on human capital development will not yield instant returns. Therefore it is also necessary to incorporate policies with short-term outcomes to ensure some political wins for the government implementing the policy, while also recognizing that short-term pains from a reform agenda could derail the process of achieving long-term goals.

CRITERIA FOR CHOICE

The CPA project provided 34 potential policy options to address the challenges in 12 broad policy areas. In an attempt to prevent instinctive personal preferences from eliminating policy choices without full consideration of their merits, I created a short-list of options. I reviewed each broad policy area, going through each policy option by section and cutting down the list in accordance with the following criteria.

First, I eliminated an option if the policy did not provide a long-term sustainable solution to the policy challenge at hand. For example, while there is a need to improve high-school graduation

rates, Riddell's proposal to increase the school-leaving age does not address whether this will actually improve student attendance (2007, 60). As Gaskell points out, it is more important to "establish[ing] schools and programs that engage students to stay involved in learning" (2007, 70).

Second, I eliminated an option if it depended on other policy options being implemented in order to be successful. Several options presented identified the need to be implemented with another option presented. Given the breath of the policy challenges, if there was an unwillingness to designate more than one option for a particular policy area, this factored into decision-making. For example, the proposal for an income tax for cities required a second policy option to restructure local governance (Slack, Bourne and Priston 2006).

Finally, I weighted policy options against alternatives based on whether the option could address a number of challenges. For example, I gave policies that had a strong human capital development component extra consideration. Therefore, it is not surprising that early childhood education (ECE) found a place in the short list, given the opportunity it presents to address several, health, equity and economic growth imperatives at once.

In pulling together a final policy package, the following parameters influenced my decisions. First, it was important that there be a balance of policies that address economic growth (efficiency) and income inequality (equity) with particular adherence to the theoretical underpinnings of endogenous growth theory. Second, the policies had to be long-term, while still considering the short-term implications for the well-being of Canadians. Third, the package had to provide a safety net for the most vulnerable in our society, in recognition of the costs to social cohesion of exclusion. Fourth, the agenda needed to be strategic in a changing global environment, with the understanding that Canada's ability to pursue prosperity and fairness is conditioned by global forces. Finally, and most importantly, the package had to consider the interaction effects among policies, leveraging complementary opportunities and mitigating perceived political unfeasibility of needed policy change.

THE POLICY PACKAGE

The final policy package identified five priorities. The reasoning behind including these priorities will be discussed below, identifying the criteria met, each policy's place in the overall package, and why other policy alternatives were dismissed. My final policy choices are as follows:

- Diversify trade: pursue free trade agreements with other countries (for example, India)
- Improve productivity: lower the marginal effective tax rate (METR) on capital investments
- Human capital development: targeted early childhood education
- Income security reform: the Caledon Institute's three-tier system
- The environment: a cap-and-trade system

1. Diversify trade with emerging global economies

Criteria met

The selection of Wendy Dobson's recommendation to diversify trade with an emerging global economy like India meets the agenda criterion of recognizing the changing global economic context. While the United States will remain our main trading partner, we must recognize that 75 percent of the world economy exists outside of the US. (Dobson 2006). India is well positioned to become a global economic power; according to one source it has "the potential to become the world's third-largest economy by 2050" (CCCE and CII 2008, 4). In addition to there being a large Indian Diaspora in Canada, Canada and India share a Commonwealth heritage, a commitment to democratic principles and a common language.

Both countries stand to gain from opening up markets for service sectors. Canada has particular strength in the financial services, information technology and engineering services, while India has strengths in software (Dobson 2006). Elevating current bilateral trade within a strategic free trade agreement will provide efficiency gains and be a long-term strategy to reposition Canada's economic competitiveness in a changing global economy.

While the details need to be fleshed out, a recent roundtable by CEOs indicates the environment is favourable for negotiation. Despite the need for further study on full bilateralization of agricultural

and cultural sectors, in particular, there are no major impediments to beginning bilateral negotiations in the near future (CCCE and CII 2008).

Conflicting criteria

There are potential consequences for the economic security of particular segments of the labour market and particular regions, conflicting with the pursuit of equity goals. This is an inherent trade-off between efficiency and equity that will occur. In order to deal with short to medium term labour market restructuring, policy option four in the package deals directly with income insecurity. Reforming income security to remove the perverse incentives and lack of coverage for working age adults is necessary to balance the potential political fallout from engaging in free trade negotiations with an emerging economy like India.

Why other policy options were not selected

Deepening integration with the United States does not appear to be a politically viable option in the near future. The US has become more protectionist lately, and further integration will provoke serious concerns on the part of policy-makers and Canadians generally about Canadian cultural and political sovereignty (Head 2007, 445). Keith Head makes a strong case that Canada has already achieved good access to the United States, and as a result there are very few low-hanging fruit left. The option to relax border administration, probably the most effective of all the US-focused trade options, would be a viable second option. However, based on recognition of global context criteria and the large Diaspora population and other commonalities between India and Canada, diversifying trade may be a more beneficial long-term strategic move.

2. Improve Canadian productivity by encouraging businesses to invest in themselves

Criteria met

Trefler (2008) and Sharpe's (2007) recommendation to lower the marginal effective tax rate on capital investments by removing the remaining provincial sales tax (PST) on machinery and equipment was selected on several grounds. First, improving productivity of Canadian businesses is crucial if we pursue a free trade agreement with an economy like India. Along with early childhood education and reforming employment insurance with a pillar dedicated to skill retraining, this policy option will work toward closing the productivity gap. According to Trefler, "Among the 15 countries with the world's highest R&D shares, Canada is dead last. And other countries, such as China and India, are hard on our heels" (2008, 1171). Improving our productivity is crucial to maintaining a competitive advantage in open trade markets.

Second, all panel critics regarded the policy as easy to implement, with positive outcomes achievable in the short-term. This policy is essentially a low hanging fruit that balances out a policy agenda with several large reforms such as cap-and-trade and a new income security system.

Conflicting criteria

In the short term, the removal of PST on machinery and equipment by harmonizing the PST with the goods and sales tax (GST) may meet political resistance from provinces that will need to increase taxes on consumer goods in order to be revenue neutral (Sharpe 2007). The benefits, however, it is estimated, would raise GDP by $1.75 billion (Drummond 2007). The suggestion that the federal government could provide some incentive to the remaining provinces should be considered pending further review (Sharpe 2007).

While this specific policy does not work directly toward equity, it is a necessary complement to a human capital development strategy to improve overall Canadian productivity (Trefler 2008). According to Trefler, if we raised per capita GDP by $5,800, this could translate into an expansion of the tax base by $68 billion dollars (2008, 1162). Improving Canadian prosperity is therefore

important in terms of improving our ability to sustain social programs and redistribute the economic pie (2008). When taken together with other policies included in the package, this would encourage the productivity and innovation required, sustaining costly programs such as a comprehensive income security system and early childhood education.

Why other policy options were not selected

Several other policy options were presented as tools to improve Canadian productivity. Developing a two-prong approach to improving prosperity by encouraging people and businesses to invest in themselves was strongly recommended (Trefler 2008). Given that two other policy options in the package had an explicit focus on human capital development (for instance, early childhood education and the Caledon Institute's three-tier reform), focusing on business was necessary to balance the overall package. While a good case was made for increasing the education of managers by investing in postsecondary education, a tax incentive to invest in capital is more direct and will yield beneficial outcomes in the short term.

3. Invest in early childhood education for the most vulnerable

Criteria met

Policy interventions that assist human capital development are beneficial on two main grounds: they improve productivity and thereby economic growth, and they address the systemic inequalities that underlie socio-economic stratification. Investment in human capital thereby provides social returns beyond private returns, requiring an active role for government, as endogenous growth theory suggests.

Investment in early childhood education may also be efficient when considering the multiple positive impacts of this policy intervention. Evidence has suggested that improved school readiness could raise returns to existing investment in education (Riddell 2007, 28). Further, reduction in crime and welfare receipt, in addition to less grade retention and special education, may present cost savings in other areas of pubic spending. In a cost-benefit analysis by the Perry

Preschool program, the estimated return to the public, approximately $7 for every dollar invested, was substantial (Riddell 2007, 29). There is also a growing body of evidence linking ECE to improved well-being, overall life satisfaction and improved health outcomes and mortality rates (Riddell 2007, 30).

Conflicting criteria

An ECE policy is a long-term human capital development strategy that may not be politically advantageous for governments on a short-term election cycle. However, it is important to note the important link between family policy and benefits to working adults. As one study points out, "Early learning and child care is an important service not only for children but also for adults, since its objectives include allowing parents to work or train or advance their education" (Battle, Mendelson and Torjman 2006, 2). Therefore, inclusion of an ECE strategy complements the policy option for three-tier reform of the income security system providing supports that make work pay (Battle, Mendelson and Torjman 2006, 28).

Finally, on equity grounds, some may argue that a targeted approach, as opposed to universal approach, would be unfair.

Why other policy options were not selected

Cost considerations and the need for better evaluation lead Riddell to advocate a targeted approach, with the possible option to expand to a universal system (2007, 34). This decision is reinforced by evidence presented by Michael Baker suggesting that causal linkages between early childhood education and the purported benefits have not been well tested. The multitude of potential benefits of an early childhood education program demand this policy be implemented and further evaluated. As Riddell says, "On balance, an early childhood education program targeted at disadvantaged children and their families seems to bring substantial benefits relative to the costs of the program" (2007, 32). As Baker and White indicate (2009), a focus on quality ECE is important for success. A targeted approach would achieve this.

4. Reform income security

Criteria met

Including a holistic reform of the income security system in the policy package meets several key objectives. First, the current income security system of EI and social assistance contains perverse incentives that effectively trap people behind the "welfare wall" (Duclos 2007). Addressing these inadequacies serves to protect the most vulnerable by preventing people from being trapped in poverty. Second, there is a need to recognize impacts on the labour market OF further opening up trade in the shorter term. Successful income security reform may help alleviate political opposition to more open trade (Duclos 2007). Finally, reallocating funding responsibility to the federal and provincial governments removes some of the fiscal squeeze currently felt by municipalities.

The three-tier reform, proposed by Battle, Mendelson and Torjman of the Caledon Institute, addresses short, medium and long-term problems associated with the current system recognizing the diversity of individuals who are presently excluded or underserved. The first tier of the system – unemployment assistance – would provide short-term support for employable adults (2006). Temporary income (TI) is a new element that would address current inequities in the system. TI would pay income-tested benefits to unemployed Canadians, many of whom are not entitled to benefits from the contributory employment insurance program (for instance, nonstandard workers, the self-employed, new entrants to the labour force).

The second tier comprises a needed focus on employment preparation (EP), which was poorly integrated into previous attempts at welfare reform, most notably the Ontario Works program (Lightman, Herd and Mitchell 2006). This tier is a medium-term approach directed only at those who have expended the TI and EI time limit and require assistance with skill development to obtain employment. The human capital focus complements other initiatives to improve productivity.

The final tier, a basic income (BI), would provide income support for individuals who cannot reasonably be expected to work. Allocating funding responsibility to the federal level would provide room for provinces and territories to finance additional supports for Canadians with disabilities

(Battle, Mendelson and Torjman 2006). This would work toward providing a safety net for the most vulnerable.

Conflicting criteria

On efficiency grounds, critics might argue that a comprehensive income security system would be costly. However, if the investments in employment preparation were done adequately, and the system served to empower rather than further marginalize individuals, there might be long run efficiencies to be gained. Most importantly, as previously outlined, an income security system that served the diverse needs of working age adults would reduce some of the political friction associated with the pursuit of more open trade.

Why other policy options were not selected

The three policy options put forward by Duclos had to be implemented together, rather than individual reforms, in order to maximize their effectiveness (2007, 249). Further, there was insufficient analysis of the potential interaction effects between EI and social assistance from singular policy interventions addressed at one pillar of the whole system.

For instance, Duclos' proposal to reform EI on insurance principles would not assist those who have worked too few hours or have repeated cycles of unemployment, if EI coverage is dependent on unemployment and contribution record (O'Hara and Sutherland 2007, 283). The proposal to implement a universal basic income is also not practical on the grounds that it does not recognize the varied needs of recipients requiring different types of support. Further, as Green (2007) says, there may still be substantial disincentives to work, and it would be too costly if BI was universal. As a result, the Caledon proposal was selected for its holistic approach to the income security system, since recognizing the interaction effects between pillars is key to successful outcomes.

5. Take action on climate change

Criteria met

With regard to climate change, the gap in governance at the federal level has led subnational governments to take their own measures toward a carbon-pricing regime (Courchene and Allan 2009). The result has been a mismatch of approaches to pricing carbon. The federal government needs to develop a strategy to deal with climate change, not only for moral and global reputation reasons, but also to prevent the long run implications for Canada's future economic competitiveness. With Alberta currently imposing a cap-and-trade system that effectively imposes an origin-based emission charge, BC and Quebec taxing consumption, and Quebec and Ontario pushing for stricter greenhouse gas controls via a national cap-and-trade, Canada is on course toward an incoherent strategy that will only heighten regional differences (Courchene and Allan 2009, 62). A national cap-and-trade system would create a single price mechanism for carbon, reducing potential inefficiencies.

While there is still a role for the provinces, the federal government is best suited to work with our major trade partner the United States in developing a system that is North American in scope (Courchene and Allan 2009).

Conflicting criteria

While the administrative feasibility of any national carbon-pricing scheme would be difficult, Canada can no longer stand to be a laggard, given the unequivocal evidence that greenhouse gases are contributing to climate change. As one environmental organization affirms, "Climate science shows that industrialized countries like Canada need to reduce their emissions by 25-40% below 1990 levels by 2020 to have a chance of avoiding dangerous climate change" (Equiterre 2008, 3).

More work needs to be done on how allowances will be auctioned and, more specifically, how Canada will approach the regionally contentious issue of the tar sands. Estimates of the potential

government revenues to be gained from auctioning allowances indicate "a broad cap and trade system covering 80% of Canada's emissions with an allowance price of $50/tonne would initially raise about $29 billion annually" (Equiterre 2008, 3). It has been suggested "money raised through the auction of allowances could be reinvested to provide targeted protection of industrial competitiveness in sectors that are demonstrably vulnerable to 'carbon leakage', ensure regional fairness, protect low income Canadians from price increases and support green technology" (Equiterre 2008, 4). The inclusion of a policy option to lower the marginal effective tax rate on capital investments would be somewhat helpful in the retooling of industries prone to emission leakage.

Why other policy options were not selected

Canada's federal government has been late to the game, and therefore does not have much credibility in pushing an alternative carbon pricing mechanism than the cap-and-trade system favoured by other countries. The Center for American Progress has been pushing for a cap-and-trade system in the United States, which appears to be getting some traction. Given our relationship with the United States and the importance of a single price mechanism in maintaining efficiency and economic competitiveness, it would make sense for Canada to follow suit.

THE MISSING PRIORITIES

Given the constraints of selecting five policy options from twelve broad policy areas, several CPA priorities are not directly represented within the package. The five policy options selected, however, were also considered because of their ability to address these excluded policy areas.

Vulnerable populations: immigrants and Aboriginal people

There are potential benefits to immigrants and Aboriginal people from an expanded income security system, as both groups run an above average risk of unemployment and exclusion from the current employment insurance system (Battle, Mendelson and Torjman 2006). However this would not adequately address the diverse needs and challenges facing both groups. An admitted

limitation of this policy package is the absence of an option that directly addresses the social exclusion experienced by Aboriginals recognizing historical injustices.

Health care

With regard to the principles of equity, health care is a priority. "For virtually every measure of health, those lower down on the socioeconomic scale have on average poorer health" (Deber 2007, 327). Health can be characterized as a special good on the basis of two principles: "(1) health is directly constitutive of a person's well-being; and (2) health enables a person to function as an agent." Health inequalities should thus be recognized as "inequalities in people's capability to function," requiring a role for government to address the systemic inequalities related to health inequity (CSDH 2007, 7).

The policy options presented in the project dealt more specifically with inefficiencies in the supply of health care and the escalating costs. While policies to reduce these inefficiencies are important, a focus on the demand-side approach to prevention is rooted in the social determinants of health literature, which looks primarily at intermediary factors that shape health outcomes (Raphael 2007, 336). Intermediary factors include psychosocial circumstances, behavioural and/or biological factors, the health system itself and, most importantly, differences in material living standards. "The material standards of living are probably directly significant for the health status of marginalized groups, and also for their lower socioeconomic position" (CSDH 2007, 35). My policy package included several policies that more broadly address the social and economic factors underlying health inequities. For instance, both the policies on income security and early childhood education might be beneficial for health outcomes, as they deal with material and psychosocial intermediary factors related to health inequity (Raphael 2007, CSDH 2007).

Cities

An agenda focused on balancing equity and efficiency needs to recognize the importance of cities as engines of the national economy, but also as places where income inequality is experienced on the ground. Our cities are vital to the future prosperity of the country (Trefler 2008). Therefore, it

may seem curious that the policy package did not include any of the policy options proposed by Enid Slack.[1] The rationale for not including an option, however, stems from the realization that if other orders of government more effectively addressed their responsibilities in the areas of education and job training, immigration, and income redistribution, cities would have the capacity to focus on service delivery and securing the vital infrastructure necessary for productive and inclusive growth. My policy package might therefore indirectly assist cities in the several ways.

Reforming income security would help reallocate some of the fiscal pressures from cities enabling them to invest more in infrastructure. In the Caledon Institute's three-tier reform, a temporary income (TI) would replace social assistance in the short term and there would be a basic income (BI) for those with longer-term need. Both of these tiers would be funded at the federal level, where an adequate tax base for redistribution exists. In Ontario a significant portion of municipal budgets is consumed by social assistance responsibilities (Slack, Bourne and Priston 2006). This has long been a concern for municipalities, and it has resulted in an underinvestment in vital infrastructure.

The TI would effectively support a reformed EI pillar based on insurance principles. A temporary income would be particularly beneficial to cities where current EI coverage is the lowest. Provincial and city differences are likely conditioned by the composition of the local labour force. For example, "areas with proportionately larger groups of new entrants to the labour force (for example, recent immigrants) – who face a higher work requirement – could see lower EI eligibility rates" (Battle, Mendelson and Torjman 2006, 18). The Caledon Institute's three-tier reform would therefore have a "considerable positive impact in Canadian cities with significant immigration and younger work forces, where Employment Insurance is not an effective instrument" (Battle, Mendelson and Torjman 2006, 30).

Growing income inequality is being realized in cities (Hulchanski 2007), targeting ECE to the most vulnerable may benefit urban areas.

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[1] The options presented by Enid Slack (2009) are, first, that the provinces should enable cities to levy an income tax and, second, that the provinces should create more effective governance structures for metropolitan regions.

Summary

My final policy package identified five priorities within the parameters of balancing the trade-off between economic efficiency and equity, and short and long-term strategies. In line with endogenous growth theory, I assigned an active role for government to address the underinvestment in goods with wider social benefits such as human capital, innovative capacity and environmental protection. In an effort to pursue a vision of Canada as a prosperous nation for all citizens, the package was created with the intention of balancing the costs and benefits of policy intervention between business and people, regions, and demographic age groups.

Moving forward, the policies need to be scrutinized in terms of costs and implementation. Regardless, the package of policies constructed has carefully considered the challenges and opportunities facing Canada in the domestic and global context, providing the starting point for a discussion of the future policy priorities this country should engage in.

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